

HOLD FOR RELEASE  
UNTIL PRESENTED  
BY WITNESS  
July 8, 2009

**Statement of  
The Honorable Ronald R. Spoechel  
Chief Financial Officer  
National Aeronautics and Space Administration**

**before the**

**Subcommittee on Government Management, Organization and Procurement  
House Committee on Oversight and Government Reform  
House of Representatives**

Chairwoman Watson, Ranking Member Bilbray, and Members of the Subcommittee, I am pleased to be here this afternoon to discuss NASA's financial management and reporting. NASA takes seriously its responsibility for reporting its performance to the citizens of the United States, the President, and the Congress, as evidenced through the many public reports in which NASA details its programmatic and financial performance.

**Financial Statement Audit "Disclaimed" Although Progress Complimented**

On an annual basis, NASA prepares a full set of financial statements that are independently audited. There are three audit reports that cover the Agency's financial statements, internal controls, and legal compliance. Since FY 2003, NASA has received a "disclaimer" of opinion from the auditors on its financial statements. While the auditors' reports for FY 2008 complimented NASA on its recent progress, as with prior years, they also noted NASA's continued inability to provide sufficient evidential support for the amounts presented in some of the accounts in the financial statements. The reports also cited two internal control material weaknesses, as well as certain non-compliance with regulatory requirements for financial systems and an inability to meet certain requirements to ensure compliance with federal accounting standards.

**New Approach Developed and Implemented in FY 2008 – Comprehensive Compliance Strategy**

In order to address the underlying problems preventing NASA from regularly obtaining an unqualified audit opinion on its financial statements, the Agency took a new approach in FY 2008 toward resolving weaknesses and improving the fidelity of its financial data, as well as expanding the usefulness of reported financial information to drive enhanced financial and operational performance. With respect to the preparation of its accounts and financial statements, this change in approach began with developing and implementing a new global financial management strategy, a Comprehensive Compliance Strategy (CCS), that focuses on ensuring full compliance with Generally Accepted Accounting Principles (GAAP) and other financial reporting requirements. The CCS serves as the basis for implementing comprehensive proactive corrective actions as may be required and it provides the guiding principles for executing effective financial

management functions and activities with internal control and compliance solutions inherently embedded in the processes.

### **Comprehensive Compliance Strategy Identifies GAAP and other Regulatory Requirements by Financial Statement Line Item**

The structure of the CCS begins with the identification of the baseline requirements by financial statement line item and account, including those on the Balance Sheet, Statement of Net Cost, Statement of Financing and Statement of Budgetary Resources. The requirements for meeting all applicable standards are identified for each of the financial statement line items and are identified in conjunction with required financial statement assertions which cover completeness, existence, accuracy, valuation, ownership, presentation, and disclosure. This serves as the foundation for identifying the evidence of auditability for each such account as required to ensure an adequate audit trail exists along with proper supporting documentation. Furthermore, the CCS addresses overarching financial reporting processes and related information technology systems. The CCS also delineates the generic control environment necessary to ensure functions and activities adhere to financial reporting requirements.

In addition, the CCS provides a solid platform for sound financial management practices and standards. Accordingly, the CCS is implemented through NASA Policy Directives (NPDs) on financial management, the associated NASA Procedural Requirements (NPRs), and the Continuous Monitoring Program (CMP). The CMP is designed to ensure that the CCS evidence of auditability flows naturally from the process, forming the Provide to Auditor (PTA) listing, and associated document generation, necessary to meet financial statement audit requirements. The alignment of CCS, the CMP, and financial management policy not only identifies actions necessary to close compliance gaps, but also provides uniform guidance that results in consistent processes, standard financial performance measurement capability, and GAAP compliance.

### **Continuously Updated**

The components of the strategy are updated on a continuous basis to ensure that the CCS remains up to date with all governing requirements, including, but not limited to, current government regulations, accounting standards, communications from external auditors and other independent oversight bodies, reviews, and assessments. These updates also become the basis for developing issue-specific corrective actions or other remediation which may become necessary for continual full compliance with GAAP and other regulatory requirements.

### **CCS Facilitates Monitoring and Oversight to Ensure Operational Effectiveness**

Monitoring and oversight of the effectiveness of the CCS is conducted through the Continuous Monitoring Program (CMP) as well as through ongoing Evaluation Monitoring and Testing (EMT) periodic compliance reviews. These monitoring tools are intended to provide another level of management assurance regarding compliance with the CCS. They also serve as a review program to periodically measure the effectiveness of the CMP, as well as ensure and validate the operation of a sound system of internal control over financial reporting.

### **Continuous Monitoring Program Provides Framework for Management Controls**

While the CCS provides the roadmap for the ongoing achievement of financial management excellence, the CMP provides the overall framework of management controls that NASA uses to

assess and evaluate internal controls, compliance with GAAP, and evidence that balances and activity reported in its financial statements are auditable.

Further, the CMP ensures that errors and/or discrepancies are identified and corrected in a timely manner. It also ensures ongoing management reviews and validations of financial data and internal controls.

### **Continuous Monitoring Program Provides Control Activities for Each Business Process and Account**

The details within each section of the CMP, referred to as Chapters, are designed to capture control activities for entire business processes for specific accounts. As a result, each Chapter may address multiple related line items in the financial statements. Each Chapter also includes the proprietary and budgetary accounts that relate to the business process. In each Chapter, control activities are defined for performing required reconciliations of each financial statement account.

Each Chapter of the CMP includes full details of the following: (i) reference to each of the financial statement line items that are supported by the section; (ii) references to each applicable general ledger account including both proprietary accounts and related budgetary accounts; (iii) management assertions to be made related to each financial statement line item and account listed; (iv) the control objectives to be met and how to detect misstatements in significant financial statement reporting assertions and Required Supplementary Stewardship Information (RSSI); (v) the GAAP financial reporting objectives that the control activities support; and, (vi) definition and applicable standards for all control activities that collectively support the management assertions, control objective, and financial reporting objective for the section.

Further, each of the control activities within each Chapter of the CMP is fully described and standards for each activity are covered as follows: (i) description of the purpose of reconciliation and any unique aspects of the activity; (ii) the frequency with which the reconciliation is to be performed (e.g., daily/weekly/monthly/quarterly); (iii) the designation of responsible reporting entity, generally either a Center or Agency Headquarters; (iv) information on the standard data sources that are to be used for the control activity; (v) information on applicable external data sources (e.g., Treasury reported confirmations); (vi) description of the transaction within the Agency's SAP financial system environment or other financial information database; (vii) the accounting periods to be analyzed, which generally are either year-to-date or inception-to-date periods; (viii) detailed explanation of the procedures and reviews to be performed; (ix) reference to valid and usual reconciling items and timing differences; and, (x) expected standards and thresholds for differences or exceptions (which may have different levels for month-end, quarter-end, or year-end financial statements).

These detailed processes and activities that comprise the CMP provide a comprehensive basis for effective monitoring and the assurance of compliance with all required and necessary control reconciliation processes at the account level.

### **Monthly Certification Process Ensures Timely Corrections and Provides Audit Documentation**

Upon the closing of the financial books each month and the preparation of the financial statements, each NASA financial reporting entity provides a matrix of control activity results and

certifies that each control activity has been performed and completed. This ensures that either results were consistent with the standards set forth for each activity or that detailed exception reports and remediation plans were prepared and implemented. Then, each month the forms are analyzed and evaluated by both Headquarters and Center management.

NASA has also implemented a rigorous quality control process to validate that control and reconciliation processes are properly performed and the reported results are supportable and accurate. When all control activities have validated performance with results as targeted, NASA will be able to demonstrate that it has management and internal controls that ensure its financial statements are reliable and have been prepared in accordance with applicable federal GAAP. The reconciliations and other procedures performed as part of each control activity also provide the supporting documentation of balances and activities needed for audit purposes.

### **Key Challenges Remain to Attaining an Unqualified Opinion**

Together the CCS and CMP provide the foundation and key compliance processes for addressing the data integrity, management oversight, and systems findings in the FY 2008 financial audit's first internal control material weakness, for financial systems, analyses, and oversight. By design, the CCS and CMP prompt the identification and elevation of any unresolved data integrity issues at NASA Centers, system configuration issues, and Agency-wide financial process issues. As these issues are identified and prioritized, corrective actions are designed to resolve them.

The data integrity issues identified through the CMP are, in many instances, related to anomalies at a specific Center, often due to past operating practices prior to the consolidation of all financial transactions into the Agency's SAP financial system. Once identified, the responsible Center takes the necessary actions to resolve the anomalies, with NASA Headquarters monitoring and assisting to ensure that prompt resolution occurs. The efficacy of the approach can be seen in the progress made as reported for the results of the CMP over time. From 210 exception reports totaling almost \$800 million (exclusive of the legacy PP&E account issues) across the Agency at the beginning of the CMP implementation in March 2008, last month showed substantial improvement with only 26 exceptions totaling approximately \$5 million.

With respect to remaining system configuration issues, NASA continues to identify and implement corrective measures for outstanding system issues. In FY 2007, a major SAP Version Upgrade was implemented, and at least twice during each year, including FY 2008 and 2009, system enhancements and upgrades were implemented. These upgrades collectively corrected a number of weaknesses identified by management and the auditors in the prior four years as well more recently identified issues. Nevertheless, fixes for many known issues remain to be implemented and the auditors continue to identify a variety of weaknesses as noted in their audit report on Internal Control. With the system corrections and enhancements which have been or are being implemented this year, NASA will significantly reduce, if not eliminate, incorrect transactions due to improper configuration or design within the Core Financial Module of its SAP financial management system.

NASA's other material weakness cited again in this past fiscal year's audit was on controls over reporting of legacy Property, Plant, and Equipment (PP&E) and materials contracts in the financial statements. For the more complex issues, like these related to NASA's PP&E reporting and systems configuration challenges, Agency-level solutions and intervention have been required. For example, early in FY 2008 NASA implemented a new policy and related procedures for identifying the cost of individual assets throughout such assets' acquisition

lifecycle. The policy change was based on guidance obtained from the Federal Accounting Standards Advisory Board (FASAB). The associated procedural changes support the verification and reconciliation of asset values for those assets created or developed under contracts awarded following the implementation of the revised policy, and also applied to certain large pre-existing contracts.

Additionally, during FY 2008, the Agency implemented a new Integrated Asset Management module within its financial management system that addresses a key part of the weakness and non-compliance with federal regulation noted in the audit report. This module is intended to provide the following benefits: (1) more accurate, timely recording and valuation of PP&E; (2) improved valuation, capitalization, and depreciation processes; (3) improved audit trail of capitalized PP&E; (4) standardization of NASA-held and NASA owned/contractor-held property management processes; (5) elimination of manual processes; and, (6) reduced operational costs.

With respect to legacy assets, however, like the International Space Station and Space Shuttles, whose acquisition began before the CFO Act of 1990 and the mandated use of GAAP accounting by the Government in FY 1998, NASA does not have the necessary supporting information available to provide *auditable* book values under current accounting standards. Together, Shuttle and Space Station related assets represent about \$19 billion of the total \$21.6 billion PP&E net asset value reported in NASA's September 30, 2008, year-end financial statements.

Although an issue for NASA at present, much of this issue may become moot with the passage of time, as the continuing depreciation of the Shuttle and Space Station assets brings the net asset balances on the balance sheet to levels that may become immaterial to the financial statements. The Shuttles are being depreciated through their expected useful life based on their current schedule for retirement in 2010 after completing the flight manifest, and the International Space Station is being depreciated based upon a 15-year specification life, through 2016. While the International Space Station depreciation schedule naturally leads to 2016 as an outside date for resolution of this PP&E issue, NASA is presently developing and evaluating a variety of alternatives with a view to achieving a timelier, albeit still cost efficient and effective, solution for this issue.

One of the alternatives the Agency has considered would involve a complete reconstruction of the original purchase invoice trail going back several decades since the inception of the Shuttle and the International Space Station programs. As NASA does not have the necessary records, it would need to rely on records which its contractors might be able to reconstruct. In addition to the considerable expense for reconstructing such an auditable invoice trail, the assurance of success is relatively low due to the low likelihood of contractors having maintained detailed and auditable records going back that far in time.

Another alternative is predicated on the Federal Accounting Standards Advisory Board amending applicable accounting standards, as it is currently considering in its exposure draft of a proposed Statement of Federal Financial Accounting Standards entitled, *Estimating the Historical Cost of General Property, Plant, and Equipment – Amending Statements of Federal Financial Accounting Standards 6 and 23*. This proposed standard, if it becomes effective, would amend existing accounting policies to clarify that reasonable methods of estimating original transaction data historical cost and accumulated depreciation may be used to value general property, plant, and equipment. As FASAB noted, use of estimates is a more cost effective means of implementing new accounting requirements than reconstructing actual historical amounts based on inadequate or non-existent accounting records. The Board further asserted that clarifying that

estimation based on adequate techniques is acceptable should promote cost effective implementation. NASA is preparing the foundational materials necessary for it to comply with the standard should it become effective and thereby allow the Agency to be in a position to provide auditable values for its Shuttle and Space Station PP&E accounts.

Nevertheless, until such time as (i) the reported net book value of these assets naturally depreciates to a level that is immaterial in comparison to NASA's other asset balances, or (ii) an auditable reconstruction of these assets' historical costs and revised depreciable values over more than a decade is performed, or (iii) applicable accounting standards change, or (iv) another of the alternatives under consideration is successfully implemented, NASA will not be able to attain an unqualified opinion.

### **Successful Implementation of Financial Management Initiatives and Continued Progress**

As noted, the Agency successfully developed and introduced a new strategy and program to ensure that financial transactions are reported consistent with applicable accounting standards, laws and federal regulations and that financial data is accurate, reliable, and auditable. The strategy has contributed to a significant decline in the number and dollar value of exception reports and a clear path forward to full compliance has been demonstrated. A new PP&E policy, an upgraded Integrated Asset Management system, and revisions to accounting processes are resulting in more consistent and reliable tracking and reporting of the Agency's property, plant, and equipment capital costs. A successful transition of much of its transactional finance operations to the NASA Shared Services Center, a focus on improvements to its grants management processes, and continuing enhancements to its underlying core financial system capabilities, coupled with improvements in the Agency's financial and performance reporting, are already providing faster, more accurate, and more usable information to drive better decisions and resultant performance across the programs and projects at NASA.

In FY 2008, NASA established the foundation for financial management excellence through the newly developed and implemented Comprehensive Compliance Strategy, Continuous Monitoring Program, and expanded financial performance capabilities. In FY 2009, the Agency is focusing on rigorous execution using this foundation to improve effective operation of financial systems and processes and to drive even better financial performance across the Agency's operations and projects. Sound financial management remains vital to NASA's success in achieving its mission, requires the combined efforts of the entire Agency, and is a priority commitment for the Agency's management.

Madam Chairwoman, thank you for your support and that of this Subcommittee. I would be pleased to respond to questions you or the other Members of the Subcommittee may have.